

COUNCIL AGENDA: 10-19-04 ITEM:

# Memorandum

TO: HONORABLE MAYOR AND CITY

COUNCIL

FROM: Leslye Corsiglia

SUBJECT: SEE BELOW

**DATE:** October 12, 2004

Approved

Date

10-13-04

COUNCIL DISTRICT: Citywide

SUBJECT: PROPOSED REVISION TO THE FEDERAL COMMUNITY

REINVESTMENT ACT (CRA)

#### **RECOMMENDATION**

It is recommended that the City Council authorize the Administration to file comments on the proposed rules issued by the Federal Deposit Insurance Corporation (FDIC) objecting to proposed regulation changes that would decrease the number of lenders and limit lender accountability to lend to low- and moderate-income communities pursuant to the federal Community Reinvestment Act (CRA).

## **BACKGROUND**

This memorandum was unable to follow the normal process of going to Rules Committee prior to being reported out to the City Council because the October 13, 2004 Rules Committee is being held as a Rules In-Lieu. Due to the deadline of October 20, 2004 to make public comments on these proposed rule changes, it was necessary to receive direction from the Mayor and City Council prior to the next formal meeting of the Rules Committee, which will take place on October 26, 2004.

#### **ANALYSIS**

In 1977, the CRA was enacted to encourage depository institutions to help their surrounding communities satisfy their credit needs, including low-and moderate-income neighborhoods. Contrary to public perception, the CRA requires that lending institutions provide loan products in lower income communities, but not that they provide loans with more favorable terms. In basic terms, the CRA was created to respond to the "red-lining," or identification, of communities where credit opportunities would not be offered.

The Comptroller of the Currency Administrator of National Banks (OCC) states that since the implementation of the law, banks and thrifts have opened new branches, provided expanded

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services, adopted more flexible underwriting standards, and made substantial commitments to increase lending to underserved populations. Current estimates stipulate that since the CRA's inception, banks and thrifts have made more than \$1 trillion in loan pledges to low-and moderate-income areas.

Under the current CRA regulations, adopted in 1994/1995, the performance of banks with assets of \$250 million or more is rated annually to scrutinize the level of lending, investing and services provided to low- and moderate-income communities. These CRA records are taken into account when banks apply to open additional deposit facilities, including mergers and acquisitions.

As indicated above, under current regulations, banks with assets of more than \$250 million must demonstrate the distribution of their loans by geography and income and must demonstrate that they provide both services and investments that benefit low and moderate income households and neighborhoods in their communities.

On August 20, 2004, the Federal Deposit Insurance Corporation (FDIC) proposed raising the asset threshold for "small banks," which are currently exempt from the Community Reinvestment Act's more stringent reporting requirements. The proposed rule would raise the small bank threshold from \$250 million to \$1 billion. A small bank threshold change from the FDIC would mean approximately 2,000 FDIC-insured institutions would have to meet a much less rigorous CRA standard. While in the City of San José only one of its thirteen banks would qualify under this revised threshold, we have serious concerns about the broader policy issue this rule change would present.

The Notice of Proposed Rulemaking issued by the FDIC states that raising the asset threshold for small banks directly supervised by the FDIC would more than halve the percentage of banks subject to the Act's lending and disclosure requirements. As of March 31, 2004, 20.9% of the FDIC-supervised banks meeting the existing threshold requirement are deemed large banks subject to the CRA requirements, and comprise 79.8% of assets. Under the proposed rule, by reclassifying more FDIC-supervised banks as small rather than large banks, only 4.3% of FDIC-supervised banks, comprising 57.9% of assets, would be required to follow the CRA lending and disclosure requirements. This is a dramatic change in potential lending partners for low- and moderate-income housing. The reduction in numbers of institutions subject to the CRA's reporting requirements also makes it far less likely to detect any "redlining."

#### **CONCLUSION**

The banks see great benefit to "streamlining" the reporting process and reducing regulatory barriers. The basis for the proposed change, according to the FDIC, is to "reduce unwarranted burden consistent with ongoing efforts to identify and reduce regulatory burden where appropriate and feasible." While this may be a good solution for banks, the Housing Department is apprehensive that a watered down version will not allow us to track the work of our lending community in San José. The Housing Department increasingly uses this data when determining the lending practices in our low-income communities and uses this data to track and guide how San José is doing in serving the needs of our residents. The Department believes that with these

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proposed changes, the current transparency of the system will be lost to the detriment of our low-income neighborhoods. Therefore, we would encourage the FDIC to reconsider the threshold of \$1 billion as the definition of a "small bank."

The FDIC is currently accepting public comments on these proposed changes. The comment period ends on October 20, 2004. The Department seeks the City Council approval of this recommendation and will file the comments immediately.

# **COORDINATION**

This memorandum was coordinated with the Intergovernmental Relations Cabinet, the City's federal lobbyist, and the City Attorney's Office.

### **CEQA**

Not a project

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Director of Housing